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**“INTERNATIONALIZATION PROCESS OF *h3* TO THE GERMAN MARKET”**

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## Executive Summary

The goal of this thesis is to make an internationalization plan of *h3* to the German Market. *h3* is a Portuguese fast-food restaurant chain mainly placed in the food courts of shopping centers serving a variety of menus with a mono-product, an hamburger. *h3* has started the internationalization process in 2011 being now present in Spain, Poland and Brazil. The success of *h3* in these countries encourages the company to keep up its expansion process. Its business can be replicated and transferable to Germany through franchising because *h3* has a standardized process in the whole chain. Since the right partnership can define the company's success, *h3* can ask Franchise Pool International (FPI) to find a master partner. Even though *h3* has to pay for having FPI's services, it is expected that these costs will be compensated by the expected gains: the fees per opened store and the royalties per percentage of sales.

**Keywords:** h3, Fast-Food, Franchising, Germany

## Business Description of *h3*

*h3* is a **Portuguese restaurant chain** emerged in **2007** which operates in the **fast food market** offering **affordable** and **quality hamburgers**. This business arose from the sales success of the hamburger *gourmet* menu offered by ***Café3***, a restaurant owned by **three friends** Mr. Albano Homem de Melo (a lawyer with experience in advertising), Mr. António Cunha Araújo (lawyer) and Mr. Miguel van Uden (real estate consultant). Even profitable, ***Café3*** was having sales returns below expectations so these three friends have decided to take advantage from the successful hamburger *gourmet* menu to come up with a new business, a **“fast food restaurant assembly line”**. Although there

are already street stores, this restaurant chain was envisioned to be present mainly in the food courts of **shopping centers** to serve a variety of menus with a mono-product - the hamburger - to enable a cost and time efficiency. The brand *h3* followed the same logic of *Café3* with “3” representing the three founders and “h” the concept name, hamburger. The blue color for the logo was chosen to trigger a feeling of freshness since it is not a common color in the fast food courts.<sup>1</sup> *h3* has also decided to register two **trade-marks** in WIPO<sup>2</sup> so that people could associate the terms “not so fast food”<sup>3</sup> and “new hamburgology”<sup>4</sup> to *h3*. They have targeted **executive young people** who value **high quality meals** served in a **short period of time**. *h3* invited Mr. Victor Lourenço, the *Café3* cuisine **chef**, to be a minority partner and to help the company with his know-how of **cooking techniques** to produce high quality industrial meals.<sup>5</sup> This chef is also in charge of “Escola de grelha”, a training program for employees to learn how to grill. Besides, *h3* has also created **manuals** for employees with standardized and systematized procedures and it is constantly stimulating them through **internal marketing activities**, like parties, that promise to be unforgettable and in which “speaking of work is forbidden”<sup>6</sup>. This is a low cost marketing strategy that *h3* found to stimulate team building and to promote the internal organizational culture.

The new business started in 2007 with two stores and the **initial investment** was €200,000 of equity and €200,000 of equipment leasing. In 2010, 12 stores were already opened in Portugal with a **franchising** strategy in the **north** of Portugal (region above Coimbra). In **2010**, *h3* had **3.2%** of **market share** in the Portuguese catering sector and

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<sup>1</sup> See in Appendix 1 the *h3* logo

<sup>2</sup> WIPO – World Intellectual Property Organization

<sup>3</sup> *h3* believes it can offer tasty food at an affordable price in a short period of time

<sup>4</sup> *h3*’s hamburgers are made with clean high quality meat, grilled and served on heated plates with metal knife and fork, contrary to the common concept of thin, frozen and tasteless hamburgers served between two slices of bread.

<sup>5</sup> See in Appendix 2 the organizational structure of *h3*

<sup>6</sup> Expression used by Mr. Nuno van Uden, marketing manager of *h3* in one of the interviews

**4.9%** of **market share** in the Portuguese Fast Food Sector<sup>7</sup> (Euromonitor International, 2011).

**Table I - Number of employees, stores and business volume from 2007-2011**

Year	Number of employees	Own stores	Franchise stores	Foreign Stores	Total Number of stores	Business Volume (in thousand €)
2007	40	2	-	-	2	341
2008	140	6	2	-	8	3.027
2009	400	17	4	-	21	10.987
2010	600	22	11	-	33	22.000
2011	700	27	12	4	43	N/A

Source: *h3*, 2011

In Portugal, *h3* has a partnership with a **distribution company**<sup>8</sup> that also works as a supplier since it is in charge of receiving the purchasing orders and buying, storing and delivering the products to the stores.

In **2011**, *h3* has opened six new stores in Portugal and it has also started the **internationalization process** with four new stores, one in Warsaw (Poland), two in São Paulo (Brazil) and one in Madrid (Spain). The first three were opened through a **joint venture** strategy and the last one through a **franchising** strategy with Vips, a leading Spanish foodservice chain<sup>9</sup>. Even though a joint venture could be safer to have more control over the business, *h3* faced some flaws in Poland as a result of not knowing the Polish local market (for example, the extra costs with the construction and design of the store by not being aware of the local law). On the contrary, a franchising strategy could eliminate this drawback and since *h3* has several manuals with standardized procedures, as well as “Escola de Grelha”, the quality management control could be easily faced. Therefore, *h3* has decided to **franchise** the company in Spain and intends to **continue** with this **expansion model** in the future. Thus, in the following years, the company

<sup>7</sup> See in Appendix 3 the evolution of *h3*’s market shares

<sup>8</sup> More information will be stated further on

<sup>9</sup> Information about the Spanish contract will be stated ahead

intends to strengthen its business in the countries where it is already present and to continue its expansion process over the years.

### Vision, Mission and Objectives

The **vision** of *h3* is to be the best hamburger chain in the world. Therefore, the firm is planning to be present in all continents within 5 years. Its **mission** is to serve a meal of excellent taste at a low cost in a short period of time. The strategic objectives of *h3* for 2012 are shown in the following table:

**Table II - Objectives of *h3* for 2012**

Domestically	Internationally	Globally
- Open 4 to 5 stores in the Lisbon area	- Open 10 stores in Madrid	- Achieve a global sales volume of 40 million Euros
- Open 4 to 5 stores in the Oporto area	- Open 3 to 4 stores in Poland	- Decrease by 10% to 15% operational losses
- Open a restaurant outside of a shopping center in Oporto	- Open 2 to 4 stores in São Paulo	- Increase the brand recognition mainly outside of Portugal through <i>word of mouth</i> , opinion makers and invitations made by <i>h3</i> .

Source: *h3*, 2011

### Purpose of the Work/Methodology

The **goal** of this thesis is to make an **internationalization plan of *h3* to the German Market**. This thesis is divided into **two parts**. The first one, worked together with other colleagues, includes the **analysis of the company** as well as the industry where *h3* is inserted. Even though *h3* has also a few street stores, this study will be **focused** on the **shopping centers' stores**. To understand who are the major competitors of *h3* and if people go on purpose to the shopping center to go to *h3*, it was created an online and food court **survey**<sup>10</sup>. To understand the business and history of the company, the group made several **interviews**: one to Mr. Albano Homem de Melo and Mr. Miguel van

<sup>10</sup> See in Appendix 5 Goals, Limitations and Results of this survey

Uden, three to a marketing manager of *h3* and one to a financial manager of *h3*.

The second part involved an individual work, in which it was prepared an internationalization **plan for Germany** - the country suggested by *h3*. To understand the German's **attitudes and habits** it was made an interview through e-mail to a German resident and other interview to a German Erasmus student from NOVA. **FPI** (Franchise Pool International), an initiative of the German Franchise Association, was also contacted through e-mail. The whole research was made through internet and supported by several **reports and publications** from different sources which will be properly referred throughout the work.

### Industry Mapping<sup>11</sup>

In the market where *h3* is inserted, a number of **relationships** take stake.

**Distribution Center** - *h3* has a distribution center in charge of buying, storing and delivering the products to the stores. This distribution center works almost as the unique **supplier** of *h3*.

**Competitors** – *h3* is inserted in the catering industry having **direct and indirect competitors**. The direct competitors are considered the fast food restaurants from the food courts that have affordable prices and a fast service. All the other restaurants are indirect competitors. Mc Donald's, Vitaminas, Noori Sushi, Go Natural, Pans&Company and Joshua' Shoarma are the main competitors of *h3*.<sup>12</sup>

**Substitutes** - The financial crisis may be considered a change condition that leads potential consumers to opt for **homemade meals**.<sup>13</sup>

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<sup>11</sup> See in Appendix 4 Industry Mapping representation as well as its explanation in more detail

<sup>12</sup> See in Appendix 5, the results of the market survey carried out.

<sup>13</sup> [http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content\\_id=1207576&page=1](http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content_id=1207576&page=1) (accessed in November 6<sup>th</sup>, 2011)

**Shopping centers** – Each store has to obey to the shopping center’s **requirements**; it has to pay the rent and to receive cleaning services from the shopping center.

**Market regulators** – *h3*’s market regulators are the respective **Municipal Council** of each store, the **DGAE**<sup>14</sup> and **ASAE**<sup>15</sup> that is in charge of accessing and communicating the risks in the food chain.

**External Auditors** – *h3* receives the services of an outsourcing company, **ControlVet** and from a “**mystery client**”, who visits the factories and stores and then evaluates the process through criteria pre-defined by *h3*. *h3* has also an audit company for equipment.

**Partners** – The know-how of **chef** Victor Lourenço is very important to adapt the homemade meals to industrial meals. He is also present in the stores’ opening (even the stores out of Portugal) and he is in charge of “Escola de Grelha”. The **meat supplier**, the **distribution center** and the **franchisees** are also considered partners of *h3* since they have helped the company in the expansion and development process.

**Customers** – *h3* has two types of customers: **business-to-business**, in which franchisees are included (in this case there is less information flow) and **business-to-consumers** addressed to its own stores and final consumers.

### **Value Chain of *h3***<sup>16</sup>

*h3* shows in its Financial Statements<sup>17</sup> of **2010** a **4% profit margin**. In the report we had access to, there were only considered the profits of the own stores and the profits related to the royalties received from the franchisees were not included. The **primary activities** comprise the assembling line and the marketing, sales and service department.

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<sup>14</sup> Direcção Geral das Actividades Económicas (General Direction of Economic Activities)

<sup>15</sup> Autoridade de Segurança Alimentar e Económica (Food Safety and Economic Authority)

<sup>16</sup> See in Appendix 7 the Value Chain representation

<sup>17</sup> See in Appendix 6 the Balance Sheet and Financial Statements’ Resume of *Café3* - Restauração SA



The **assembly line** contributes to **31%** of *h3* total costs and it includes the wages of the stores' employees and the costs with food preparation, hygiene, cleaning, repair and maintenance of the stores as well as the wastes associated to those stores. The **marketing, sales and service department** is in charge of the advertising and the control of the royalties received from the use of the brand. These activities only represent **5%** of the total costs since *h3* bets on *word of mouth* to publicize the brand. The **secondary activities** include: the firm infrastructure, human resource management/technology and procurement. The **firm infrastructure** includes the management costs (consulting, auditing, legal costs etc.) representing **25%** of the total costs. The **procurement activity** includes the stores and offices' rents and the Distribution Center responsibility of purchasing, storing and delivering the raw materials, as well as the quality management. Overall, it represents **34%** of the total costs. The **human resources management and technology development** activities have been analyzed together since *h3* does not have a department specialized in technology development so people in charge of this task also have other responsibilities. These costs represent **3%** of the total costs and comprise the personnel costs (office employees' wages) and all the costs with technology development.

Sofia Ribeiro Telles, one of the managers of the Financial Department of *h3* has told us that the company considers a priority to **decrease** the **raw materials** and **distribution costs** as well as the **wastes** associated. With economies of scale, the company is also able to **take advantage** of its **bargaining power** to negotiate prices and quantity discounts. More difficult to **reduce**, are the **human resources management costs**. This would be possible by decreasing the number of employees per store but to avoid a firing process the company could **reallocate** some **employees** to the new stores.

### Sustainability Factors and Competitive Advantages of *h3*

Several factors ensure the domestic and international **sustainability** of *h3* namely: the operations' **standardization** that enables the time and cost efficiency, the strong **brand recognition** which helps the company to have access to the distribution channels and to establish good partnerships, the **stores' location**, placed in areas with great influx of people, and finally the **menus' alignment** to the **population habits**. The competitive advantages include the characteristics that distinguish a company from its competitors. In the case of *h3* there are **two competitive advantages**. The first one is the **customization** of the own dish. In fact, even though *h3* has already defined several menus, consumers are free to personalize their plate choosing a rare or well-done hamburger as well as the desired side orders (sauces, chips, rice, vegetables etc.). The **price/quality relationship** is also a competitive advantage since *h3* was able to create a *gourmet* concept at a very affordable price. The quality of its hamburgers as well as its different types of side orders (for example, its original and fresh round chips or its *thai* rice) lead the consumers to perceive *h3* as being a food chain that offers a **homemade meal** with a great emphasis on flavor and quality. The combination of the quality of its ingredients together with the affordable prices and the fast response service observed, makes the price/quality relationship an important source of advantage that distinguishes *h3* from its competitors.

### Fast Food in Portugal<sup>18</sup>

According to the market analyst Datamonitor, the fast food market is defined as the sale of food and drinks for immediate consumption either on the premises or in designated

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<sup>18</sup> See in Appendix 8 information about the growth percentage of units, transactions and value sales in the Portuguese consumer foodservice from 2005-2010 and the forecasts for 2010 until 2015

eating areas shared with other foodservice operators, or for consumption elsewhere. This market is divided into four segments: Quick Service Restaurants (QSR), Takeaways, Mobile & Street Vendors, and Leisure<sup>19</sup> (Datamonitor, 2010). In 2010, the fast food sector increased 3% in Portugal, reaching 715 million Euros. McDonald's is the leader chained operator with 53% market share. The Burger fast food continued to be the most important category with sales value of 337 million Euros. Even though 2010 was not the best year for the most fast food chains to increase the number of stores, *h3* was able to distinguish itself from the others with a significant expansion. The fast food sector is expected to grow by 2% CAGR<sup>20</sup> in constant value representing 792 million Euros by 2015 (Euromonitor International, 2011).

### Porter's 5 Forces<sup>21</sup>

**Barriers to entry** – Even though the initial investment is relatively low (around €200,000) and there are low switching costs, the fast food market is in the mature stage and it is difficult to get access to shopping centers and to build a new brand recognized in the market. Furthermore, the cost efficiency needed to succeed in this market may scare away potential entrants. The current financial situation also complicates the disposal of bank loans and the interest rates are very high. Besides, the legal requisites of food quality certification may also constitute a barrier to new entries since they can lengthen the process of opening a new restaurant. Therefore there are **medium/high barriers to entry**.

**Threats of substitution** – The threat of substitution through homemade meals is increasing with the financial crisis<sup>22</sup>. People are avoiding eating out to save money.

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<sup>19</sup> See in Appendix 9 the market definition

<sup>20</sup> CAGR - Compound Annual Growth rate

<sup>21</sup> See in Appendix 10 the main conclusions of Porter's Five Forces

Thus, there is a **medium threat of substitution**.

**Buyers' bargaining power** – Although there are greater levels of substitution due to the financial crisis and low switching costs associated, the buyers have **low bargaining power** due to the low volumes purchased per customer and because within the fast food market, *h3*'s customers show a lower price sensitiveness caused by its price/quality relationship.

**Suppliers' bargaining power** – As it was already said, the company considers it has only one supplier, the **Distribution Center**. Since *h3* is highly dependent on it, this supplier's **bargaining power** is very **high**. Besides, there are also the suppliers of exclusive products, like the **meat supplier**. They are quite dependent on the volumes purchased, but on the other hand, *h3* also depends on them since a change of supplier would result in higher costs. Therefore, these last have a **medium bargaining power**.

**Competitive Rivalry** – on one hand *h3* is able to reduce rivalry by attracting customers due to its good price/quality relationship and it can also benefit from the fast-food industry growth. On the other hand, this industry is very competitive since there are numerous competitors with a very strong reputation and there are low switching costs. Thus, the **competitive rivalry of this industry is high**.

### TOWS Analysis<sup>23</sup>

#### Taking advantage from strengths to maximize opportunities

- The standardization of procedures and the learning curve facilitate the expansion of *h3* through franchising

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<sup>22</sup> [http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content\\_id=1207576&page=1](http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content_id=1207576&page=1) (accessed in November 6<sup>th</sup>, 2011)

<sup>23</sup> See in Appendix 11 SWOT Analysis

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- Key partners of *h3* can also be seen as a brand strength since they are able to help the company expanding. Chef Victor Lourenço with his know-how of cuisine techniques helps *h3* in the adaptation of homemade meals to industrial food and gives employees' training; the franchisees help *h3* with their investment capacity and know-how on franchising and the local market; the meat supplier and the distribution center are able to respond to the company's growth.
  - *h3* provides meals with fresh and quality ingredients which can lead consumers to perceive the company's meals as healthy food. The trade marks "new hamburgology" and "not so fast food" also help the public to get this idea.
  - The good price/quality relationship of *h3* is a good way to face the economic crisis. In fact, customers may start to turn to this type of solutions.
  - The brand awareness *h3* has built over the years in Portugal, facilitates the negotiation and entry in the Portuguese shopping centers
  - The training programs for employees increase the stores' capacity of delivering the meals in a short period of time, enabling the company to respond to the fast food consumption growth.

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#### **Taking advantage from strengths to avoid threats**

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- The standardized production and distribution processes lead to a bigger cost and time efficiency facilitating the competition with the rivals as well as the implementation of a take-away service.
  - *h3* should bet on promotion strategies to take advantage from its learning curve experience and avoid any threat from the strong reputation of its competitors.
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### Minimizing weaknesses to avoid threats

- By offering a mono-product *h3* faces a serious threat in a situation of cow disease. Therefore the company should start producing soya or vegetarian hamburgers.
- *h3* should bet on market research to minimize weaknesses and avoid threats.

### Taking advantage from opportunities minimizing weaknesses

- Even though the food courts' environment is sometimes seen as not very pleasant, *h3*'s stores benefit from the great influx of people. Since the number of shopping centers is increasing in Portugal, *h3* should continue to position itself in these places.
- The franchising model can be a good way to face the potential problems the company faces when the tactics and strategies are not well defined by the board.
- To meet the market opportunities, *h3* should bet on market research

### Germany's Fast Food Sector<sup>24</sup>

In **2009**, the German fast food market **grew** by **3.4%** reaching a value of \$5,982.1 million that corresponds to a CAGR<sup>25</sup> of 3.8% for the period between 2005 and 2009. In the same year the market volume grew by 1.1% that worth 2,346.1 million transactions. In **2010**, Germany accounted for **17.5%** of the **European fast food market value** with the Quick Service Restaurant being the largest segment of the fast food market, reaching 58.7% of the market's total value (Datamonitor, 2010). In **2010** the **fast food market increased** in value by **5%** compared to the previous year mainly due to Germany's underway recuperation from the global economic crisis, which led many German consumers to eat out more frequently than previously (Euromonitor International,

<sup>24</sup> See in Appendix 12 the World Market Analysis of the Fast Food Sector

<sup>25</sup> CAGR – Compound Annual Growth Rate

2011). In **2014**, the **German fast food market** is forecasted to have a value of \$7,080.7 million and a volume of 2,501.2 million transactions, corresponding to an **increase compared to 2009** of 18.4% and 6.6%, respectively (Datamonitor, 2010). Fast food outlets are increasingly attempting to overcome the threat of the ongoing **rise** in the **health** and the **wellness trend** among German consumers by introducing healthier menus (Euromonitor International, 2011).

### Porter's Five Forces for Germany

**Barriers to entry** - it is not required great capital expenses to enter in Germany. Through franchising the expansion costs are reduced since with a minimum capital of €25,000, the franchisor may build a private limited liability company (GmbH) (Metzlaff, Karsten and Tom Billing, 2011). Even being in a situation where consumers face low switching costs, a competitor with a strong brand awareness, may lead the entrant to waste any effort in achieving success. The legal requisites of food quality certification may also constitute a barrier to new entries since they can lengthen the process of opening a new restaurant. Nevertheless, according to Datamonitor, optimistic growth rates are expected in the following years (CAGR of 3.4% from 2009-2014) so there is a **moderate likelihood of new entrants**.

**Threat of substitution** - The main factors for choosing fast food may be the convenience and availability together with the value allocated to the consumer needs. Therefore, its substitutes comprise other ways of profit foodservice and also ready meals or ingredients for home cooking that give the consumers greater freedom to control the diet (Datamonitor, 2010). Thus, substitutes constitute a **moderate threat**.

**Suppliers' bargaining power** - The suppliers also play an important role in the

Germany's fast food sector. The fast food chains generally require an acceptable quality of raw materials with very low margins achieved with high volumes purchased, but the fact that suppliers have different types of customers makes them less dependent on the fast food companies, strengthening their power (Datamonitor, 2010). Therefore, they assume a **moderate power**.

**Buyers' bargaining power** - Despite a decline in the consumer expenditure and the signs of market saturation, the investment in the fast food industry remains high, with new stores opening across the sector (Datamonitor, 2010). Thus, the consumers' power seems to be **moderate**.

**Competitive Rivalry** - McDonald's remained the leading brand in the German fast food market during 2010, accounting for 5% of total fast food outlets. In 2010, the fast food chains with higher brand shares were Mc Donald's with 58.8%, Burger King with 14.9% and Nordsee with 5.5%<sup>26</sup> (Euromonitor International, 2011). To face the economic crisis, the industry players are delivering cheaper value offerings to encourage consumers to eat out of home. As already said, the profitability relies a lot of times on low margin-high turnover operations forcing the competition through price. Players are betting more on differentiation through brand awareness, value pricing and food quality trying to have a direct impact on customers' loyalty, and ultimately weakening their bargaining power. Even though the intensity of competition may be softened by the lack of high exit costs, the rivalry is considered to be **strong** (Datamonitor, 2010).

### **Germans' attitudes and habits<sup>27</sup>**

According to a research developed by Bord Bia in 2008, 46% of German adults have

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<sup>26</sup> See in Appendix 13 a table with the Brand Shares of the Fast Food Chains in Germany from 2007-2010

<sup>27</sup> See in Appendix 14 the interviews.



full time working jobs and 29% of Germans eat in the workplace several times a week. Nevertheless, Germans are **eating out more often during the week**, mainly male and younger adults (**18-34 years old**). Primary reason for midweek eating out is related to the chance of meeting with friends. This segment is the one that attends more to cafes/bars and uses takeaway and food delivery services (Bord Bia, 2010). In Germany, the majority of fast food restaurant customers consume their meal within the outlet, with only **27%** choosing to **take** their order **away**; however this is an increasing trend. Fast casual dining is an emerging trend and it has become especially important due to the rise of the health and wellness trend (Euromonitor International, 2011). According to Ms. Ingrid Kronsbein, a German resident, “people start working very early, usually between 7a.m. and 9a.m. leaving between 3.30 p.m. and 6p.m.. Many people have **short time for lunch**, a lot of times around half an hour, so they often cannot go to a restaurant. Large companies usually have a **canteen** with a choice of meals, where most people go. The people who work in small companies without canteen, usually go - if they have time – to a **small restaurant** with a set of meals at an affordable price (between €6 and €10) or go to a **fast-food** restaurant such as Mc Donald’s, Turkish, Italian or Chinese. Who works near **shopping centers**, may also go there for lunch. Many people also **bring food from home**.” Roman Friedrich, a German Erasmus student from NOVA also said that even though home cooking is “pretty loved” by Germans, Germany is a nation of “**restaurant visitors**”. In his opinion *h3* may succeed in Germany since, with the exception of Jim Block, there are no quality fast food chains in Germany and if *h3* is able to convince consumers about its price-quality relationship, there will be a positive reaction to its entry.

## Mode of Entry

**Franchising**<sup>28</sup> is very popular in the fast food sector in Germany and the majority of chained international fast food players in Germany operate a higher proportion of their outlets under franchise in comparison with other countries because it gives them the opportunity to expand quickly (Euromonitor International, 2011). To enter in the German market, *h3* would have a safer approach if choosing a **franchising strategy similar** to that used in **Spain**. In fact, according to the study “Franchising – A guarantee for success for business start-ups”, which was published by the International Center for Franchising and Cooperation (F&C) at the University of Münster in 2005, the failure rate among franchised businesses is considerably lower than among traditional business start-ups. Therefore, *h3* could apply a “**business format franchising**”, in which, the franchisee would pay *h3* the rights to use their expertise, knowledge, trade name, trade mark and logo as part of a business enterprise. Doing so, *h3* would be **expanding** its operations at a **low cost** and **low risk** and still retaining the control over its business idea with the power to apply new control arrangements over the franchisees to protect the franchise system. *h3* would **receive** a one-off **fixed sum** and then **fees** based on turnover. This strategy would also be riskless for **franchisees** since they would **benefit** from an already **proven business model** and at the same time they would face less bureaucratic barriers if starting as a normal start-up (Perlitz, 2008). I think a franchising strategy would work for *h3* in Germany because its business idea shows a clear market potential, already proven by the Spanish expansion success. In fact, one of the *h3* advantages is the process **standardization** that **allows** the business concept **replication** and therefore its **transferability** through franchising. Of course, this will only be

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<sup>28</sup> See in Appendix 15 the definition of franchising

possible if the German market is able to accept new franchisees so that the franchise system can achieve an optimal size or scale (Ahlert et al., 2008). This is confirmed by a 2008 Deutsche Bank Research, in which is stated that franchising has nearly tripled its nominal turnover in Germany. And one explanation was the high rates of expansion of the fast food franchising sectors.<sup>29</sup> Until 2015, even in a slower rate, the sector turnover is expected to grow by 7% p.a., around 70 billion Euros (Bord Bia, 2008).

### German Market Access

Germany, like most European countries, operates under the **civil code system** that had stimulated the harmonization of trade, tariffs, legal requirements, standards and procedures. In general, franchising agreements are subject to the laws governing commercial contracts. When operating in Germany companies are expected to honor the “**European Code of Ethics for Franchising**”, defined by several trade associations and by recently implemented EU regulations in which it is agreed the relationship between the franchisor and the individual franchisee (U.S. Commercial Service Germany, 2005). Legislation specifically relating to franchising consists of several legal statutes and codes that must be observed when establishing a franchise agreement in Germany. Of great importance is the "**Deutsches Lebensmittelgesetz**" (German Food Law, 15 Aug. 1974), a federal law that is supplemented by numerous individual regulations and is regarded as particularly strict, often being used as a legal model for corresponding **EU-regulations**. All imported goods have to meet the requirements of the act, with federal and state laboratories conducting obligatory analyses of the product (U.S. Commercial Service Germany, 2005). While other countries have fixed by law the

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<sup>29</sup> See in Appendix 16 a graph with the franchising turnover being higher than the German GDP growth

amount of briefing to be given by the franchisor, the **commitment to disclosure** in Germany is based on a **mutual trust agreement**, in which both parties commit themselves to lay open all the relevant information to the future cooperation.<sup>30</sup> The transmission of the information should be in writing and in the German language.<sup>31</sup>

An essential, but often neglected part is the **commercial legal protection**, such as trademarks, patents and registered designs which are given to the franchisee for his use. The **trademark protection** can be done by registration at the German Patent Office in Munich (Franchise Verband, 2011).

### Expansion of *h3* to Germany

For many international franchise systems, the question arises as to how the available business model can be successfully transferred to a new country. The adaptation of the franchise model to local cultural realities and good national contacts play an important part. Finding the **right master franchisee** can define the success of expansion in a new market. This franchisee should have several **characteristics** such as: the necessary **capital resources** for acquisition of the license and financing the cost of sales so as to reach the break-even point of the system center; it should have **management skills**, an excellent **network** of contacts, managerial **experience** in order to successfully direct the existing franchise system in the long term and it should have strong **communication skills** in order to gain franchise partners for a (still) new system. The **Franchise Pool International**, an initiative launched by the German Franchise Association (DFV - Deutscher Franchise Verband) could **help h3** in **finding** the **master partner** who would

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<sup>30</sup> See in Appendix 17 more details about the Mutual Trust Agreement

<sup>31</sup> See in Appendix 18 the documentation needed prior the closure of the franchising contract

best fit with the company business.<sup>32</sup> In just five years, Franchise Pool International has attained the position as market leader in international master franchise recruitment in Germany. The Pool has official members in UK, Scandinavia, Holland, Austria, Czech Republic, Romania, Adria region and Italy. *h3* could request a “**recruitment service**” from this network of independent franchise experts specialized in the brokerage of franchise systems in international markets. They would support *h3* in the **preparation** of the expansion plan to Germany as well as on the **search** for **suitable partners**. *h3* would be subject to a study of the business feasibility in the respective country. *h3* could also obtain the help of a **lawyer** from the **German Franchise Association** specialized in the German franchise law (Franchise Pool International, 2011). Mr. Rolf Kirst, board member of the International Franchise Affairs and the German Franchise Association explained that if *h3* chooses the services of FPI, it is mandatory to have available a sophisticated and successful business concept, full franchise documentation for international sales, realistic calculations for a franchise outlet, professional support and training offer for the master, professional and usable manuals, reasonable number of franchisees in the home country and their testimonials. To help *h3* to prepare this information FPI offers a **strategy workshop** for international systems together with other franchise consultants.<sup>33</sup>

### Franchising contract of *h3* with the selected master partner

*h3* could define a **contract similar** to that established in 2011 with the Spanish Group, **Vips** in which it could give to the selected partner the exclusive exploitation right of *h3* in Germany and the possibility to sub-franchise under some conditions. The menus’

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<sup>32</sup> See in Appendix 19 the process of finding the best match between the company and the master partner

<sup>33</sup> See in Appendix 20 information given by Mr. Rolf Kirst about the content of this workshop

prices would be suggested by the partner and subject to approval by *h3*. *h3* would define the value of the **entry fee** and the master partner would **receive all the *h3*'s manuals**.<sup>34</sup>

In the contract would be also included the values of the **fee per opened store** and the **royalty value** which would vary with the percentage of sales. According to *h3*, this parameter can range from 5% to 10%, depending on the contract and country. If they sell X, they have to pay 5%, if they sell X+Y they have to pay 6% etc. Since in Spain this parameter is between 5% and 10% and in Portugal 4% and 8%, the minimum limit percentage should be higher than 5% for Germany because the CPI (Consumer Price Index) of Germany is higher than in Portugal and Spain (Central Statistics Office, 2011). As reported in the Spanish contract, the German master should also have at least 60% of own stores having the possibility to **sub-franchise 40%** of them. Since it was agreed the opening of 10 stores in Spain until 2012, *h3* should open more **stores**<sup>35</sup> in Germany in the first year since Germany has a much higher population density, higher annual net earnings, higher purchasing power and higher GDP per capita than Spain.<sup>36</sup>

Besides, Germany fast food sector is expected to grow by 3.4% until 2014. Like in Spain, the **two first stores** would be exclusively **designed by *h3***, with Portuguese architects in charge of the functional part and the presence of the Portuguese art director of *h3* who would design the entire store image. The goal would be to **train a German architect team** to start to design the following stores. *h3* would also guarantee the **training** of the **employees** of the **first two stores** but the third store would already be the master partner responsibility. It would also be defined in the contract that the master franchisee would be able to give training hours to other master franchisees if needed,

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<sup>34</sup> *h3*'s manuals: store management manual, a store opening manual, a training manual, an operating manager manual, a supervisor manual, a service manual, a cuisine manual and a manual of grilling.

<sup>35</sup> See in Appendix 21 the reasoning for suggesting *h3* to define in the contract the opening of more stores than Spain in Germany in the 1<sup>st</sup> year

<sup>36</sup> <http://epp.eurostat.ec.europa.eu/portal/page/portal/eurostat/home/> (accessed in November 13<sup>th</sup>, 2011)

being this clause part of a global strategy that could help *h3* to avoid higher costs in the future. In the agreement it would also be stated that the master franchisee would have the support of a **Portuguese country manager** who would be entirely dedicated to Germany. In the beginning of the expansion process, the meat and the rest of the ingredients could come from Portugal but in the future, the Portuguese country manager would be in charge of **searching and finding** the best **suppliers** and a **distribution center** in Germany in order to reduce the transportation costs.

Like in Spain, the **marketing campaigns** should be **paid** by the **franchisee**. They would be exclusively developed by *h3* in the first two stores and for the other stores, it is required the *h3* approval to guarantee that the campaign is aligned with the concept. Besides, the **master partner** has to present at least **two campaign initiatives per year**, all the rest is defined by *h3* and each store adapts the idea to the respective local area.

### **In which German cities should *h3* start to be present?**<sup>37</sup>

At the end of 2010, Germany had 437 shopping centers. Since 1999 the number of shopping centers has increased by 57% with the growing number of shopping centers being in the city centers, suburbs of the towns and in the centre of secondary cities<sup>38</sup>. So, if *h3* expands to Germany, it will have a plenty of shopping centers' options to choose from. *h3* should start to be present in Berlin, Frankfurt and Munich. *h3* would certainly gain from having stores in **Berlin** since this is the **Germany's largest city** and the **seventh most populous** urban area in the **European Union**.<sup>39</sup> **Frankfurt** is the **leading financial centre** of Germany and it was ranked 6<sup>th</sup> among global cities for

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<sup>37</sup> See in Appendix 22 suggestions of shopping centers where *h3* could be present

<sup>38</sup> <http://www.rakli.fi/attachements/2011-04-13T14-40-3286.pdf> (accessed in November 2<sup>nd</sup>, 2011)

<sup>39</sup> <http://en.wikipedia.org/wiki/Berlin#Economy> (accessed November 2<sup>nd</sup>, 2011)

economic and social innovation by the 2thinknow Innovation Cities Index in 2010.<sup>40</sup>

**Munich** presents the **strongest economy** as well as the **lowest unemployment rate** (5.6%) of any Germany city. This city is the centre for biotechnology, software and other services. Munich is also the home of the headquarters of many large companies. Among German cities with more than 500,000 inhabitants, the **purchasing power** of this city is the **highest** (26,648 Euros per inhabitant as of 2007).<sup>41</sup>

### Implementation Plan

With the intention of going abroad it is important to design an **implementation plan**. It was established a plan with a duration period of **2 years** with the required activities and their time frame for the successful expansion of *h3* to Germany. The plan **starts in January 2013**.

**Men** – *h3* will be in charge to recruit the **employees** for the first **two stores**. The master partner will have this role for the following stores. *h3* will need to assign the role of **country manager** to a Portuguese employee who would be in charge to visit the country once in a while to check if all the procedures are being implemented.

**Money**<sup>42</sup> – *h3* Portuguese owners will have **no costs with employees**, being the franchisees' responsibility to support these costs. Like in Spain, the costs *h3* incurs in the beginning with the need for a team of architects for the construction and design of the first two stores will be entirely **supported** by the **master franchisee**. This also happens with the **training** programs. *h3* will have **costs** with the **recruitment service** of FPI and the **strategy workshop**. It will have to pay to FPI 25% of the master license fee (minimum of €30,000), €1,000 per candidate accepted and €1,000 monthly retainer fee.

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<sup>40</sup> <http://en.wikipedia.org/wiki/Frankfurt> (accessed November 2<sup>nd</sup>, 2011)

<sup>41</sup> <http://en.wikipedia.org/wiki/Munich> (accessed November 2<sup>nd</sup>, 2011)

<sup>42</sup> See in Appendix 23 additional information about the fees and the duration of the contract with FPI



*h3* would also face an additional cost with the **salary increase** of the employee with the role of **country manager** and it should also have into account his **travelling costs**. On the other hand, from the selected master partner, *h3* Portuguese owners will **receive** an **entry fee**, a **fee per opened store** and **royalties** per percentage of sales.

**Table III– Activities’ duration and dependency of the Implementation Plan**

MINUTE		
Activity	Duration	Dependency
1: Contact FPI for a “Recruitment Service”	1-2 months	
2: Participate in the Strategy Workshop offered by FPI	2-4 months	Activity 1
3: Hire a Lawyer specialized in Franchising	1-2 months	
4: Contact and sign the contract with the selected partner	3-6 months	Activity 1,2,3
5: Design and build the first two stores	3-6 months	Activity 4
6: Give the training programme to employees of the first two stores.	2-3 months	Activity 4
7: Adapt some recipes to German tastes	4-12 months	Activity 4

Source: Primary data, 2011

**Table IV– Implementation Plan’s objectives, measurement, target and initiatives**

MEMO				
	Objectives	Measurement	Target	Initiative
Financial	- Increase number of stores. - Increase revenues	- Sales revenue - Sales volume - Fee per opened store - Royalties	- Achieve the number of stores defined in the contract. - Increase revenues from royalties by 50% after 2 years	- FPI recruitment service - Partnership with Master Franchisee
Customer	- Being recognized in Germany	- Market research - Number of website visits	- 50% awareness after one year	- Marketing strategy - Webpage with information for the customer
Employees	- Recruit German employees for the two 1 <sup>st</sup> stores	- Employees’ performance accordance to company's goals	- Train all employees between 2 to 3 months	- Translate manuals to German - Recruitment and Training
Learning	- Adjust menus to German tastes	- Customers’ Satisfaction	- Increase volume of sales	- Training by the cuisine chef

Source: Primary data, 2011

## Contingency Plans

Without an **expert master franchisor**, *h3* would not be able to succeed in the German market because the information will not be correctly transferred to the German franchisees. So if the selected partner does not show the important characteristics already mentioned, like substantial financial basis, management skills and enough managerial experience, *h3* should contact FPI to solve this problem. If FPI does not respond to the company needs, the company should withdraw from the contract and try itself to find other type of strategy, not putting aside the possibility of still having a franchising strategy. *h3* should also guarantee that the adequate **monitoring and control procedures** are taking place. If this is not happening, *h3* should intervene and demand explanations from the selected partner. If *h3* is not having great **acceptance near the German consumers**, *h3* should invest in a market research to understand if the problems are the stores' location, *h3*'s offerings, its service etc. and after that it should try to adopt strategies to increase customers' satisfaction. On the other hand, if the company is not achieving the desired levels of **market recognition**, it should adopt a similar strategy used in Miraflores, a Portuguese *h3* store, in which it were given to a number of regulars of that area, invitations to eat on that store. It is expected that, like in Miraflores, this initiative triggers a *word of mouth* phenomenon. If the invited people feel satisfied with the experience, they would want to repeat it and recommend it to others. This would increase the brand recognition and since people usually trust more on the others' recommendations rather than on the company's communications, more people would want to experiment the menus.

## Conclusion and Recommendations

With the study made about the German market it can be concluded that it would be a **good decision** to **expand** *h3* to Germany starting in January 2013. In fact, the fast food **sector** is **attractive** since it is expected an increase in the market value and market volume until 2014. *h3* should bet on **take away** service as well as **delivery service** in order to be able to take full advantage of its market potential. Besides, it could also consider starting to **produce soya or vegetarian hamburgers** to protect itself from the risk of a cow disease and also to reach a greater number of potential consumers. In this research it was suggested that *h3* has the support of **FPI** services to guarantee the right partnership and an adequate expansion process. By **franchising** its business in Germany, *h3* would be using a growth strategy with low capital requirements and it would benefit from a master partner with know-how on the German culture and the fast food sector. In conclusion, *h3* has all the conditions to be successful in Germany.

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A Work Project, presented as part of the requirements for the Award of a Masters  
Degree in Management from the NOVA - School of Business and Economics

# Appendix

**“INTERNATIONALIZATION PROCESS OF *h3* TO THE GERMAN MARKET”**

Mariana Assis Teixeira Neiva Correia

Number 678

A Project carried out on the Management course, under the supervision of:

Professor Sónia Dahab

Professor Filipe Castro Soeiro

Lisbon, January 6<sup>th</sup>, 2012

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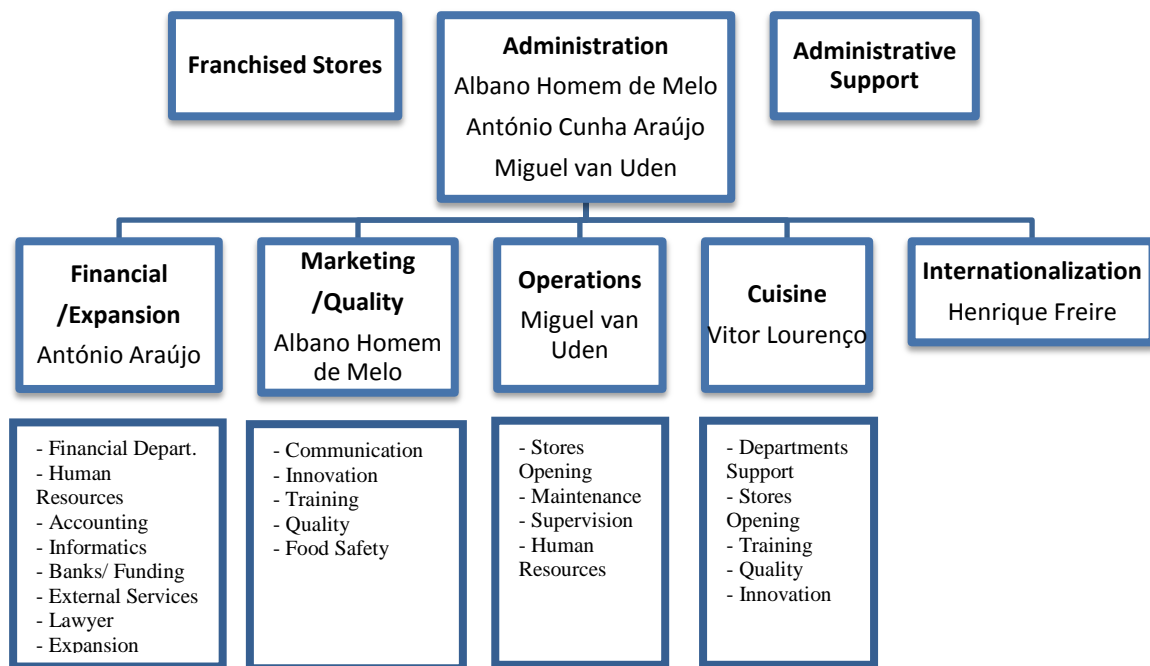


## Appendix 1: Logo of *h3*



**Figure 1** – Logo of *h3*

## Appendix 2: Organizational Structure of *h3*



Source: *h3*, 2011

**Figure 2** – Organizational Structure of *h3*

## Appendix 3: Market Shares' Evolution of *h3*

**Table I** – Market Share Evolution of *h3* in the Portuguese Catering Sector

Brand	Global Brand Owner	2007	2008	2009	2010
<i>H3</i>	<i>Café3</i> Restauração SA	0.8	1.0	1.8	3.2

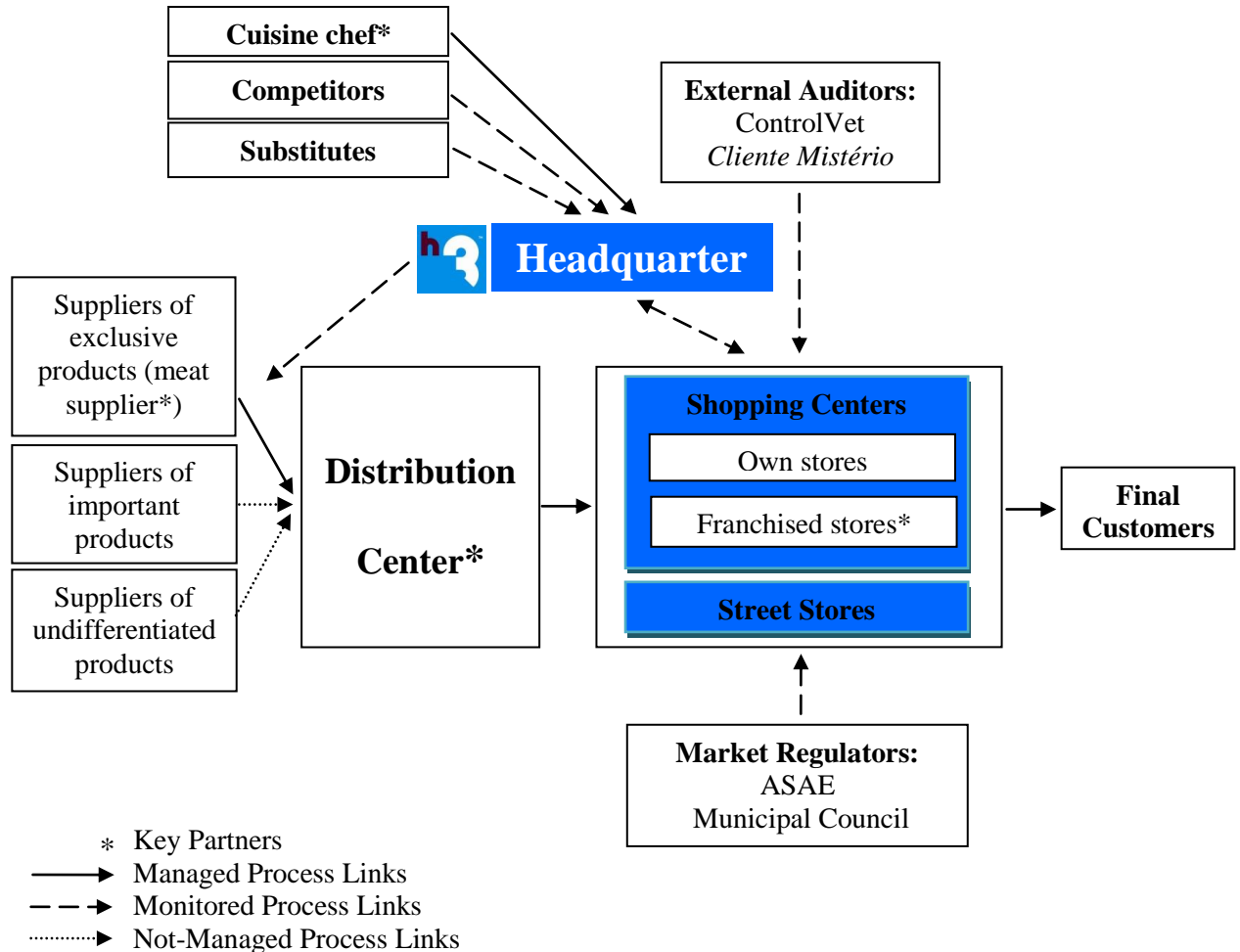
Source: Euromonitor International, 2011

**Table II** – Market Share Evolution of *h3* in the Portuguese Fast Food Sector

Brand	Global Brand Owner	2007	2008	2009	2010
<i>H3</i>	<i>Café3</i> Restauração SA	1.3	1.5	2.8	4.9

Source: Euromonitor International, 2011

#### Appendix 4: Industry Mapping of *h3*



Source: Primary data, 2011

**Figure 3** – Industry mapping of *h3*

**Managed Process Links** – links that are managed by the focal company

**Monitored Process Links** – links that are not critical to the focal company but they are important to be integrated in the supply chain.

**Non-Managed Process Links** – links that the focal company delegates totally

**Distribution Center** - Since the beginning, *h3* felt the need to find a way to control all its suppliers and the best solution it found was by having a partnership with a distribution company that would be in charge of buying, storing and delivering the products to the stores. Each store formalizes the request directly to the distribution company through e-mail with a copy to *h3*'s headquarters. The distribution center has different responsibilities according to the type of product *h3* supplies. There are three types of products: exclusive, important and undifferentiated. The suppliers of exclusive products, like the meat supplier, are chosen by *h3* and in this situation the distributor is required to buy the products to the chosen supplier. *h3* collaborators go to the factory, they define and approve the desired exclusive product and they negotiate and agree a price with the supplier. After that, this information is transferred to the distribution company that will be in charge of buying the product to the chosen supplier at the agreed price. In the case of important products, like the potato, *h3* just requires the distributor to buy a specific type of that product, being the distributor free to choose the supplier. The other products like sugar, salt and pepper can be selected by the distributor without *h3* intervention. The main advantages of this partnership for the distribution company is the fact that it can resell the products to *h3* stores with a margin and besides, since this distribution company is also a supplier of some products, it also gains from the sale of its products. *h3* saves from not having a physical warehouse and it also benefits by not having the responsibility for stock management.

**Substitutes** - substitute goods are goods which, as a result of change conditions, may replace each other in use or consumption.<sup>1</sup>

**Market regulators** – to license the stores, *h3* has to present a declaration in the

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<sup>1</sup> [http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content\\_id=1207576&page=1](http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content_id=1207576&page=1) (accessed in November 6<sup>th</sup>, 2011)

respective municipal council and a copy to the DGAE<sup>2</sup>, in which it takes the responsibility to meet all the requirements appropriate to the activity.<sup>3</sup> ASAE<sup>4</sup> is the specialized administrative authority within the national food security and economic surveillance which is in charge of accessing and communicating the risks in the food chain, as well as the discipline of economic activities in food and non food sectors, through the monitoring and prevention of compliance with regulatory legislation.

**External Auditors** – The quality management is the responsibility of *h3*. It begins with the factory approval until the production method and final product analysis. After that *h3* receives the services of an outsourcing company, ControlVet, a company that provides audit services (quality and hygiene) to *h3*, evaluating in an impartial and strict manner the compliance of the requirements defined in accordance with international standards and the company internal norms. It is also mandatory the existence of a company in charge of controlling pests, in the case of *h3*, the company belongs to ControlVet Group.<sup>5</sup> Also working as an external auditor, *h3* stores may be subject of a “mystery client” service, who visits the factories, the stores, the distribution company and its trucks and then evaluates the process through criteria pre-defined by *h3*. Besides, *h3* also has an audit company for equipment.

## **Appendix 5: Goals, Limitations and Results of the online and food court Survey**

**Goals-** The major goal of this survey was to understand who are the major competitors of *h3* and if people go on purpose to the shopping center to go to *h3*. The survey was

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<sup>2</sup> Direcção Geral das Actividades Económicas (General Direction of Economic Activities)

<sup>3</sup> <http://www.portugalglobal.pt/PT/InvestirPortugal/GuidoInvestidor/EnquadramentoLegal/Paginas/HaumprocessodelicenciamentoespecialparaaberturadeumestabelecimentocomercialPortugal.aspx> (accessed in October 13<sup>th</sup>, 2011)

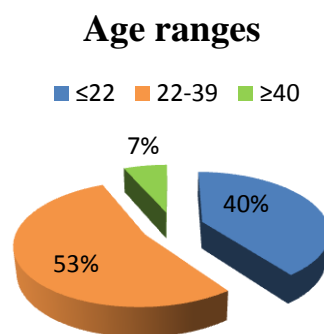
<sup>4</sup> Autoridade de Segurança Alimentar e Económica (Food Safety and Economic Authority)

<sup>5</sup> <http://www.controlvet.pt> (accessed in October 15<sup>th</sup>, 2011)

composed by four questions: gender (Female or Male); age (<22; 23-39; >40); “Do you go to a shopping center just to go to *h3*?” (Yes or No); “If you did not go to *h3*, which other restaurant would you choose? (choose between 2 to 4 options)”;

**Limitations of the Survey** - The survey has a number of limitations that must be considered when reading the data. The survey is not a representative sample of all people that go to shopping centers’ restaurants. It was used a web survey tool, *Survey Monkey*, so the results represent only those people who chose to respond to the survey. The participants in the online survey were not selected at random since the people asked to answer the survey were friends and family members of the group so this can introduce biases in the results obtained.

**Results of the Survey** - The results show that 51% of the people who answered to our survey were females and most of the people were between 23 and 39 years old as it is possible to observe in the graph shown below:



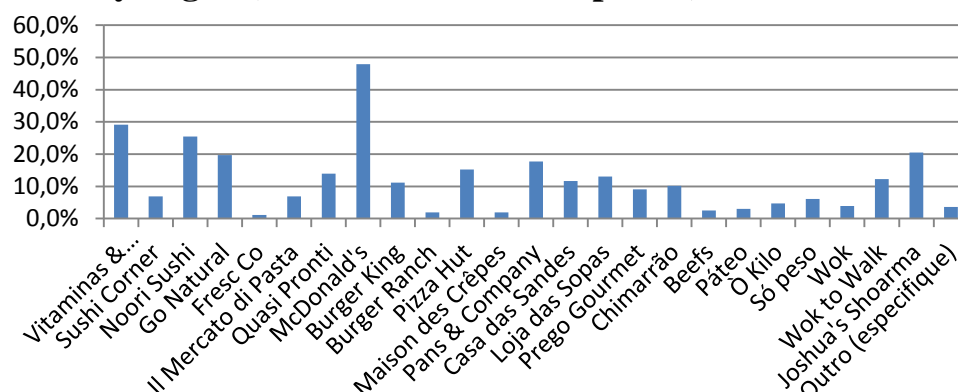
Source: Survey Research, 2011

**Figure 4** – Age ranges of people who answered the Survey

According to our survey, more than half of the people (52,4%) goes to a shopping center just to have a meal in *h3* and most of the people choose Vitaminas&Company,

Noori Sushi, Go Natural and Mc Donald's if they do not go to *h3*.

**If you did not go to *h3*, what other restaurant would you go? (choose between 2-4 options)**



Source: Survey Research, 2011

**Figure 5** – Answers to the survey about the competitors of *h3*

**Appendix 6: Balance Sheet and Financial Statements of *Café3* – Restauração SA**

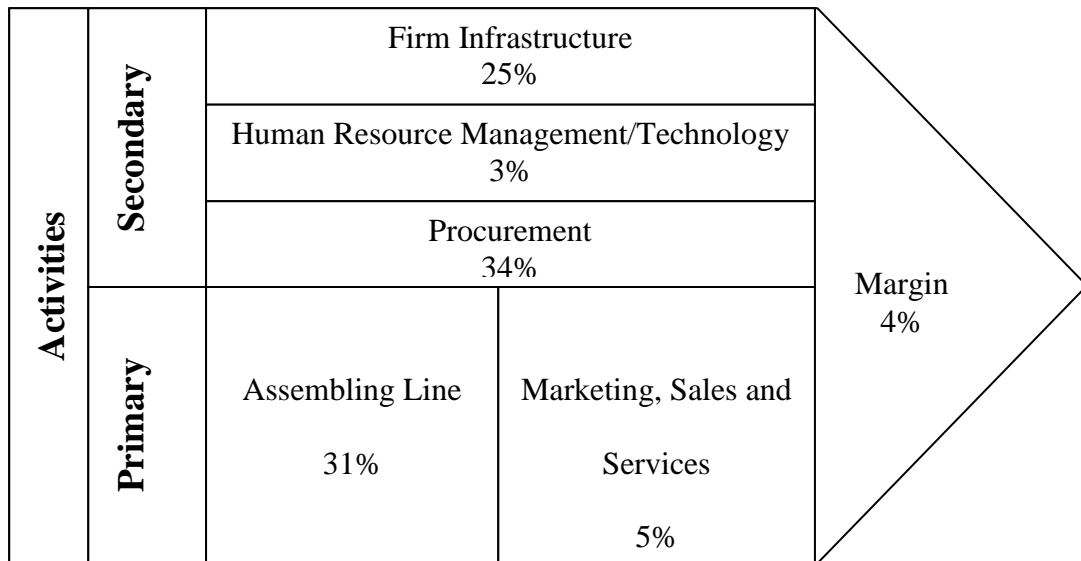
**Table III** – Balance Sheet of *Café3* – Restauração SA

(in Euros)	2007	2008	2009	2010
Imobilizações Incorpóreas	22.459,30	103.129,25	795.802,84	722.902,98
Imobilizações Corpóreas	265.039,56	785.805,85	2.419.895,34	2.929.084,08
Existências	2.875,36	45.560,20	76.353,31	261.908,52
Dívidas de terceiros - curto prazo	26.276,02	41.173,57	153.480,21	1.090.375,34
Depósitos bancários e caixa	27.659,62	341.132,71	363.427,18	374.704,32
Acréscimos e Diferimentos	3.272,28	89.105,06	194.413,48	245.664,28
<b>Total do Activo</b>	<b>347.582,14</b>	<b>1.405.906,64</b>	<b>4.003.372,36</b>	<b>5.624.639,52</b>
<b>Capital Próprio</b>	<b>6.129,41</b>	<b>88.436,14</b>	<b>669.001,14</b>	<b>886.153,39</b>
Dívidas a Terceiros - médio e longo prazo	78.315,93	580.687,61	1.346.459,72	1.199.807,19
Dívidas a Terceiros - Curto Prazo	210.605,21	597.754,17	1.614.921,39	3.538.658,94
Acréscimos e Diferimentos	52.531,59	139.028,72	372.990,11	0
<b>Total do Passivo</b>	<b>341.452,73</b>	<b>1.317.470,50</b>	<b>3.334.371,22</b>	<b>4.738.466,13</b>
<b>Total do Capital Próprio e Passivo</b>	<b>347.582,14</b>	<b>1.405.906,64</b>	<b>4.003.372,36</b>	<b>5.624.619,52</b>

**Table IV – Financial Statements’ Resume of *Café3* – Restauração SA**

(in Euros)	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
<b>Resultados Operacionais</b>	5.744,45	108.205,99	592.111,59	859.035,69
<b>Resultados antes de impostos</b>	-5.186,99	96.498,27	420.059,72	799.256,22
<b>Resultados Líquido do Exercício</b>	-5.230,89	88.517,77	294.565,00	556.171,36

## Appendix 7: Value Chain



Source: *h3*, 2011

**Figure 6 – Value Chain of *h3***

## Appendix 8: Portuguese Consumer Foodservice Data

**Table V - Units, Transactions and Value Sales in Consumer Foodservice: % Growth 2005-2010**

% Growth	2009/2010	2005-10 CAGR	2005/2010 Total
<b>Units</b>	-1.2	0.7	3.4
<b>Transactions</b>	-2.7	-1.6	-7.8
<b>Value current prices</b>	-2.4	-0.8	-4.1
<b>Value constant prices</b>	-3.7	-2.5	-12.0

Source: Euromonitor International, 2011

**Table VI - Forecast Units, Transactions and Value Sales in Consumer Foodservice: % Growth 2010-2015**

<b>% Growth</b>	<b>2010-15 CAGR</b>	<b>2005/2010 Total</b>
<b>Units</b>	0.4	2.1
<b>Transactions</b>	1.1	5.5
<b>Constant Value</b>	2.2	11.5

Source: Euromonitor International, 2011

### **Appendix 9: Market Definition**

The Quick Service Restaurants are defined as the locations where the primary function is to provide full meals but where the table service is not offered; Takeaways are defined as establishments that provide freshly prepared food for immediate consumption; Mobile & street vendors are defined as either individual mobile stalls or vans that offer a limited range of freshly prepared food as well as beverages; and Leisure Locations are defined as locations serving food and drinks for immediate consumption on premises within leisure outlets (such as Cinemas, Theatres, Racecourses etc.) that the leisure operator owns and operates itself. The market is valued through Operator Buying Prices, which is the amount spent by foodservice operators on the food and drink they serve. All currency conversions were performed using constant 2009 average annual exchange rates. The fast food market was analyzed taking fast food operators as players. The key buyers were taken as consumers, and food ingredients providers and workforce providers as the key suppliers (Datamonitor, 2010).

### **Appendix 10: Main Conclusions of Porter's Five Forces**

Assuming that this model does not take into account the market dynamics as well as the different degrees of relevance of these five forces on this particular industry, the main conclusion achieved is that even though *h3* is inserted in an industry quite competitive,



the significant level of substitution is compensated by the perceived price/quality relationship of *h3*. The considerable barriers for new entries as result of its learning curve experience are also important for *h3* since they constitute a guarantee that there is less possibility of entering a competitor with a similar concept. And the dependence of *h3* on suppliers could be minimized with a very well defined contract that ensures some level of confidence.

## **Appendix 11: SWOT Analysis**

### **Strengths**

- Focus on a single product (mono-product) – the process standardization enables cost and time effectiveness
- Easy monitoring of the production process and its employees
- Fresh and quality ingredients
- Consumers can customize their own dishes – they can choose the hamburger well-done, medium or rare and choose the preferred side orders (vegetables, chips, rice...)
- Good price/quality relationship
- Key partners: cuisine chef who shares his know-how with employees; franchisees with investment capacity and know-how on franchising and the local market; the suppliers of exclusive products, such as the meat supplier, that help the company to expand, being prepared for a sales volume growth; and the distribution center that shows a clear efficiency and control over the needed products, their storage and delivery.
- Corporate team structure enables a good communication flow – the informal structure felt in this company (board members are from the same family) enables the problems' resolution at anytime
- Branding and Creativity

- Strong training program for employees – specific tasks assigned to each employee
- Registration of “new hamburgology” and “not so fast food” in the WIPO – a good way to guarantee that these expressions would only be associated to this brand.
- Learning curve – the *h3*’s experience and acquired know-how complicates the copy of the concept.

### **Weaknesses**

- Only one meat type – may not be reaching other potential consumers
- Since most stores are located in shopping centers, the consumers may feel that the environment where *h3* is located is not very pleasant
- No table service in the restaurant
- Since the corporate team members are really close to each other, sometimes they do not formalize all the company tactics and strategies
- Lack of market research

### **Opportunities**

- Increase of shopping centers in Portugal (Cushman & Wakefield, 2010)
- Increase of the Fast Food consumption (Euromonitor International, 2011)
- Trend towards selecting healthy food (Euromonitor International, 2011)
- Economic crisis increases the need for cheap meals (Euromonitor International, 2011)
- Franchising model increasingly applied to the fast food industry (Euromonitor International, 2011)

## Threats

- The fast food market is in the mature stage with a significant variety of restaurants
- Potential epidemics of cow diseases
- European trend towards food to go or take away may arrive to Portugal<sup>6</sup>
- Main competitors are well-expanded international companies (Euromonitor International, 2011)
- Main competitors offer more variety of menus and additional services (Euromonitor International, 2011)
- The VAT (value added tax) for the catering sector increased 10%, being now 23%<sup>7</sup>
- With the economic crisis people have less income so there is a higher trend to take meals at home.<sup>8</sup>

## Appendix 12: World Market Analysis of the Fast Food Sector

Between 2005 and 2009 there was a significant growth in the fast food market with the Quick Service Restaurants being the far most lucrative segment in 2009, with a total revenue of \$142.6 billion, corresponding to 70.9% of the market's overall value. The takeaway segment also contributed to a 12.1% of the market's aggregate value with a revenue value of \$24.3 billion in the same year. In 2009, the global fast food market grew 3.1% to achieve a value of \$201.1 billion, showing a compound annual growth rate (CAGR) of 4.8% between 2005 and 2009. For the same period, the European and Asia- Pacific markets faced a CAGR increase of 4.7% and 6.1%, respectively, achieving \$34.2 billion and \$71.6 billion in 2009. The market consumption volumes faced a

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<sup>6</sup> <http://www.igd.com/index.asp?id=1&fid=2&sid=2&cid=630> (accessed in November 5<sup>th</sup> 2011)

<sup>7</sup> <http://aeiou.expresso.pt/maioria-aprova-iva-de-23-na-restauracao=f691080> (accessed in November 30<sup>th</sup>, 2011)

<sup>8</sup> [http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content\\_id=1207576&page=1](http://www.jn.pt/PaginaInicial/Economia/Interior.aspx?content_id=1207576&page=1) (accessed in November 6<sup>th</sup>, 2011)

global and European CAGR of 4.6% and 1.3%, respectively, between 2005 and 2009 and a respectively total of 208.1 billion and 12.3 billion transactions in 2009 (Datamonitor,2010).

The global fast food market has been decelerating in recent years as a result of the worldwide economic depression. Until 2014, the market performance is expected to decelerate with a forecasted CAGR of 3.6% for the period between 2009 and 2014, which will lead to a \$239.8 billion market value by the end of 2014. For the same period, the European and Asia-Pacific markets are expected to grow with CAGRs of 4.1% and 5% respectively to achieve the respective values of \$41.9 billion and \$91.2 billion in 2014 (Datamonitor, 2010).

### **Appendix 13: Brand Shares of Chained Fast Food in Germany between 2007-2010**

**Table VII – Brand Shares of Chained Fast Food in Germany between 2007-2010**

Brand	Global Brand Owner	2007	2008	2009	2010
Mc Donald's	Various franchisees	42.7	41.9	45.1	46.9
Mc Donald's	McDonald's Deutschland Inc	16.1	15.6	13.0	11.9
Burger King	Various franchisees	12.0	12.7	11.9	11.6
Nordsee	Nordsee Fisch-Spezialitäten GmbH	6.3	6.0	5.7	5.5
Subway	Various franchisees	3.1	4.3	4.6	4.9
Burger King	Burger King Deutschland GmbH	3.6	3.7	3.5	3.3
BP/Aral Petit Bistro	Various franchisees	3.7	3.6	3.4	3.1
Shell Select	Various franchisees	1.7	1.7	1.9	1.8
Esso Shop	Various franchisees	1.4	1.4	1.3	1.2
KFC	Various franchisees	0.9	0.9	1.0	1.1
KFC	Yum! Restaurants International Inc	0.8	0.8	0.9	1.0
Café Bonjour	Various franchisees	0.8	0.9	1.0	1.0
Yorma's	Yorma's AG	0.7	0.7	1.0	1.0
Espresso Ciao Agip	Various franchisees	0.9	0.9	1.0	1.0
Janny's	Various franchisees	0.5	0.5	0.5	0.5
Kochlöffel	Kochlöffel GmbH	0.5	0.5	0.5	0.5
Steigenberger Gastronomie	Steigenberger Hotels AG	0.6	0.5	0.5	0.5
Wienerwald	Various franchisees	0.6	0.4	0.4	0.4
Kochlöffel	Various franchisees	0.4	0.4	0.3	0.3

Gosch	Jürgen Gosch Verwaltungs GmbH	0.3	0.3	0.3	0.3
Sushi Factory		0.2	0.3	0.3	0.3
Häagen-Dazs	Various franchisees	0.3	0.3	0.3	0.3
Gosch	Various franchisees	0.2	0.2	0.2	0.2
Dunkin' Donuts	Various franchisees	0.2	0.2	0.2	0.2
Wienerwald	Wienerwald GmbH	0.2	0.2	0.2	0.1
Sushi Circle	Sushi Circle Gastronomie GmbH	0.2	0.1	0.2	0.1
Eiscafe Piccoli	G + G Gelato GmbH & Co KG	0.1	0.1	0.1	0.1
Aral Pananino	Various franchisees	-	-	-	-
BP Petit Bistro	Various franchisees	-	-	-	-
DEA	Various franchisees	-	-	-	-
Others		1.0	0.9	0.8	0.9
<b>Total</b>		<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: Euromonitor International, 2011

## Appendix 14: Interviews

### Interview to Ingrid Kronsbein – German Resident

- Questions

- Quais são os hábitos alemães de comer fora de casa?
- Onde costumam os trabalhadores almoçar? Em Portugal não existe muito o hábito de comer “à secretária”. Na Alemanha existe este hábito? Há quem vá à zona de restaurantes dos centros comerciais?
- O facto do *h3* ser um restaurante sem serviço de mesa não seria um problema?
- Como pensa que seria a reacção dos Alemães à chegada deste restaurante?
- Na sua opinião, quem seriam os tipos de frequentadores deste restaurante?
- Quais consideraria serem os competidores do *h3*?

- Answers

“O ritmo de vida está completamente diferente do ritmo de vida em Portugal. O trabalho começa bastante mais cedo de manhã (normalmente entre as 7 e as 9 horas) e acaba entre as 15.30 e 18.00 horas). As pessoas têm muito menos tempo para almoçar - por

exemplo uma meia hora (o que é completamente normal). Como não dá para ir ao restaurante, as grandes empresas têm normalmente uma cantina com uma escolha de refeições. As pessoas que trabalham em pequenas empresas sem cantina, vão (se tiverem tempo) a um pequeno restaurante (que hoje em dia tem pratos do dia a um preço acessível - entre 6 e 10 Euros) ou vão a um restaurante de fast food como o McDonald's, restaurantes turcos, italianos, chineses. Muitas pessoas também trazem a comida da casa porque à noite cozinham em casa.

Aqui temos centros comerciais, mas muito menos do que em Portugal. Quem trabalhar perto destes centros, também pode lá ir almoçar. Eu penso que os frequentadores deste tipo de restaurante poderiam ser os jovens, mas normalmente as pessoas aqui gostam mais de serviço de mesa quando vão ao restaurante. Competidores deste tipo poderiam ser os restaurantes de fast-food conhecidos no mundo inteiro como KFC, Burger King etc.”

#### Interview to Roman Friedrich – German Erasmus Student at NOVA

##### **- What are the eating habits of Germans outside their home?**

I have to say that home cooking is pretty loved by Germans. Not only traditional, also international and the Asian kitchen becomes more and more trendy. But anyways, Germany is a Nation of restaurant visitors, they like to go out for dinner. Not really the traditional, it is the Italian and Spanish kitchen which is pretty demanded.

In terms of fast food or “not so fast food”: McDonald's, BK, KFC etc. are also places to go or to drop by, but a “higher” quality fast food chain does not really exist (exception Jim Block). I think the idea of *h3* would attract Germans.

**- Where the workers usually have lunch? In Portugal there is not much the habit of eating at the “desk”. In Germany do you find this behavior? Are there any people that eat in the food courts of the shopping centers?**

It is pretty common to bring the own lunch to the offices and heat it up for example in the micro wave if the company does not have a canteen, otherwise the canteen is common. It is not likely that workers are going somewhere by car or a longer distance to lunch. If there is a restaurant nearby they might go there. It is also common to order lunch and let it bring by the delivery to the office, especially Asian and Pizza are preferred.

**- Do you think is it a problem *h3* does not have a table service?**

I do not see a problem at all in not having a table service in Germany in this branch.

**- How do you think would be the reaction of Germans to the entry of *h3*?**

I think they would question first the quality. The quality-price relationship needs to fit. If *h3* can convince with the quality and service (in this case its clean and structured appearance), in my eyes Germans would react very positively to the entry of *h3*.

**- In your opinion, which would be the type of patrons of this restaurant?**

Families with less time (they want a “healthy” fast meal), Business people and Students.

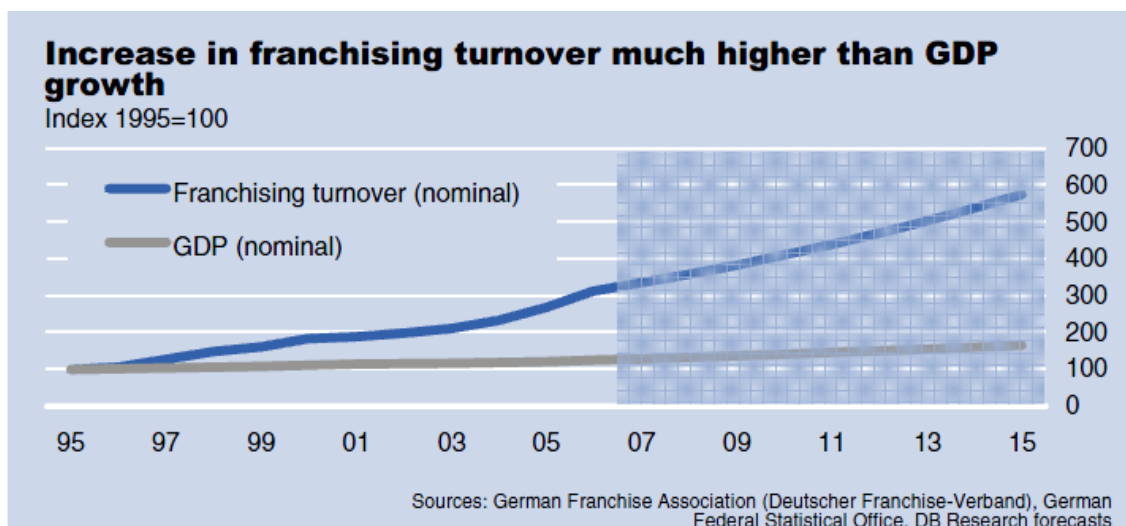
**- What restaurants could be *h3* competitors in Germany?**

Jim Block (Block House Group, in the northern area)

## Appendix 15: Definition of franchising

The European Franchise Federation defines franchising as “the basis of a contractual agreement between two independent business parties, the franchisor and the franchisee, in which the franchisor grants the franchisee, for the term of the contract, the right to buy and operate the franchisor’s branded and formatted business system for a fee and according to the prescribed rules and procedures developed for the system by the franchisor.”<sup>9</sup> This partnership is set out in a contractual franchise agreement which will define in detail all the rights and duties of both parties. Based on *h3* accumulated experiences, the franchisees will have available a manual that would enable them to replicate the business concept. Furthermore, *h3* also provides a set of services to support the franchisee’s efforts namely property rights, marketing, the provision of general agreements with suppliers, training, supervision and consulting, market information or quality management. (Ahlert & all, 2008).

## Appendix 16: Increase in franchising turnover higher than GDP growth



**Figure 7 – Increase in Franchising Turnover higher than GDP growth**

<sup>9</sup> <http://www.eff-franchise.com/spip.php?rubrique6> (accessed in October 30<sup>th</sup> 2011)



## **Appendix 17: Mutual Trust Agreement<sup>10</sup>**

The franchisor should present the prospects of success with reliable information (statistics, labor and capital requirements) so that it can enable the potential franchisee to estimate the necessary expenditures involved, to get an idea about the time-span of start-up losses and to gain a realistic view of his chances of making a profit. The franchisor should also give the potential franchisee access to the manual prior to binding agreements and the franchisee should have the possibility to assess the franchise contract and the related documents within a reasonable time frame of a minimum of ten days prior to signature of the contract (Franchise Verband, 2011).

## **Appendix 18: Documentation needed prior to the franchising contract closure<sup>11</sup>**

**1. Information concerning the franchise concept:** Company name and location of the franchisor; Business occupation of the franchisor; Date of foundation of the franchisor; Excerpt from the commercial register or trade registration; Number of company-owned businesses; Date of the beginning of franchising; Number of franchise partners; Number of newly won franchise partner within the last year; International experience.

**2. Information concerning the people with decision-making power in the system's head office:** Executive board or manager, possibly the head of the franchise department, contact persons for the franchisees (name, position, responsibility).

**3. Franchise offer:** Location, owner, duration of the pilot project (if applicable); Results and experience from the pilot project (if applicable); Services of the system's head office; Commercial protection of the intellectual property of the franchisor;

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<sup>10</sup> [http://www.franchiseverband.com/fileadmin/user\\_upload/MAIN-dateien/English/4-documents-for-downloads-12\\_Disclosure\\_Guidelines.pdf](http://www.franchiseverband.com/fileadmin/user_upload/MAIN-dateien/English/4-documents-for-downloads-12_Disclosure_Guidelines.pdf) (accessed in November 2<sup>nd</sup> 2011)

<sup>11</sup> Information given by Mr. Rolf Kirst, board member of the International Franchise Affairs and German Franchise Association

Marketing concept of the franchisor; Franchise fees; Necessary special training of the franchisee; Information concerning the necessary equity requirements of the franchisee. This applies to initial investments during the start-up phase as well as thereafter.; Necessary general labor input of the franchisee (if applicable); Key economical numbers of comparable franchise outlets of the system.

#### **4. Outlook on profitability, if available**

#### **5. Franchise contract (including all standardized attachments)**

**5.1. Bank references:** Name and address of the bank; Bank connections

**5.2. Information on memberships in professional associations:** Addresses and duties of the associations; Duration of the membership; Status.

**5.3. Information on other distribution channels of the franchise products or services:** Branches, wholesale trade, specialist trade, mail order, structure sales, internet sales etc.; Sales to company clients and large customers through the franchisor.

### **Appendix 19: Process of finding the best match<sup>12</sup>**

Within the framework of FPI marketing activities, potential founders are generally and usually addressed across the system itself. In addition to that FPI uses the following means of communication on a case by case basis: publishing systems information in online media newsletter, working with founder networks, presentations at founder events, cooperation with organisations and associations, FPI internet presence, publicising the system in several franchise web portals, additional promotion in web portals on demand, editorial articles in franchise magazine, processing queries from interested parties generated by the franchise system, the positioning of the franchise

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<sup>12</sup> Information given by Mr. Rolf Kirst, board member of the International Franchise Affairs and German Franchise Association

system in the German founder market, presentation of the company at trade fairs by FPI, display of notices in online and printed media specially for the franchise concept within the framework cited above; design, organization, implementation and follow-up of group presentations; design, organization, implementation and follow-up of assessment centers for potential candidates; compilation of a personality profile for the candidate.

FPI assumes the preparation and pre-selection of all parties interested, which have heard about the franchise system through FPI's or systems marketing activities. FPI assumes the following basic activities: sending documents to potentially interested parties by e-mail, following up all potentially interested parties by reminder e-mail or with a phone call, bearing all general communication costs (telephone, fax, etc.), inviting for personal profile questionnaire.

After qualifying interested parties, Franchise Pool International will follow up with the candidate as follows: telephone pre-qualification of all interested parties, telephone discussion about the franchise concept, qualification of all interested parties potentially suitable for a franchise partnership with the franchise system through a personal conversation and checking and assessing of the basic motivation of the parties concerned. Finally, personal presentation of the franchise system as part of a one to two-hour headline presentation to inform interested parties about the franchise system in detail. If the qualified and in principle suitable party is interested in meeting the management of the franchise system, FPI will present the candidate to the franchisor. As part of the preparation for the presentation, the franchise system will receive a '*Founders profile*' compiled in English for each interested party which contains all relevant information from the initial conversations and all personal data given by the

candidate. This enables the franchise system to reach a decision about whether it wishes to meet the interested parties.

## **Appendix 20: Content of Strategy Workshop<sup>13</sup>**

The content of the workshop would be: system success factors for Germany; Franchise performance analysis of the system; Strategy discussion; Review the franchise package for a master; Tools and material for franchise sales; Franchise agreement and manuals; Recruiting process; Financial calculations; Time planning and future steps. As a result of this workshop it will be prepared:

1. **Strategy plan** for the roll out in Germany - Kind of license (Master, multi unit, single); Ways of promotion and marketing; Recruitment process; Fee structure; Legal documents

2. **Profile** for potential master franchise candidates with reference to their specialist and personal competence; professional background; equity provision; basic motivation; suitability as franchise partner; suitability as entrepreneur

3. **Franchise disclosure documents** given by FPI to potential new master franchise partners about the franchise system during the various stages of the acquisitions process. This includes various information about: the activity of the franchise company, the history of the franchise company, the market and sector of the franchise system in general, the key success factors of the franchise system compared to its competitors, business model of a franchise operation, activities of a franchise partner, financial key data of a franchise operation, draft of the agreement

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<sup>13</sup> Information given by Mr. Rolf Kirst, Board member of the International Franchise Affairs and German Franchise Association

## Appendix 21: Number of stores to be opened in Germany

To suggest the number of stores *h3* should open in Germany in the first year, it was used as basis of comparison the number of stores defined in the Spanish contract with Vips, 10 stores in the first year of contract. So, several economic indicators were analyzed to compare these two markets and based on that achieve a conclusion about the optimal number of stores to open in Germany in the first year.

**Table VIII** – Annual net earnings, population density, purchasing power parities and GDP per capita of Spain and Germany

	Spain	Germany	Observation
Annual net earnings <sup>14</sup>	15,861.45	24,908.99	Data from 2010
Population Density <sup>15</sup>	90,8	229,9	Data from 2008
Purchasing Power Parities <sup>16</sup>	0,932209	1,05268	Data from 2010
GDP per capita in PPS <sup>17</sup>	100	118	Data from 2010

Source: Eurostat, 2011

As it is possible to verify, Germany has higher annual net earnings, higher population density, higher purchasing power and higher GDP per capita in relation to Spain. Therefore, together with the expected growth of 3.4% of the German fast food

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<sup>14</sup> **Annual Net earnings** - Information on net earnings (in absolute figures) and related tax-benefit rates (in %) complements gross-earnings data with respect to disposable earnings. The transition from gross to net earnings requires the deduction of income taxes and employee's social security contributions from the gross amounts and the addition of family allowances, if appropriate.

<sup>15</sup> **Population Density** - The ratio of the mid-year population of a territory on a given date to the size of the territory.

<sup>16</sup> **Purchasing power parities (PPPs)** are indicators of price level differences across countries. PPPs tell us how many currency units a given quantity of goods and services costs in different countries. PPPs can thus be used as currency conversion rates to convert expenditures expressed in national currencies into an artificial common currency (the Purchasing Power Standard, PPS), eliminating the effect of price level differences across countries.

<sup>17</sup> **Gross domestic product (GDP)** is a measure for the economic activity. It is defined as the value of all goods and services produced less the value of any goods or services used in their creation. The volume index of GDP per capita in Purchasing Power Standards (PPS) is expressed in relation to the European Union (EU-27) average set to equal 100. If the index of a country is higher than 100, this country's level of GDP per head is higher than the EU average and vice versa. Basic figures are expressed in PPS, i.e. a common currency that eliminates the differences in price levels between countries allowing meaningful volume comparisons of GDP between countries

sector in 2014, it is reasonable to propose a greater number of stores to be opened in Germany in the first year than the number defined in the Spanish contract.

*h3* should also take into account the financial capability as well as the experience of the master partner since they may constitute an important factor to define the number of stores to open in this country.

## **Appendix 22: In which Shopping Centers to franchise?**

Zeil is the Frankfurt's central shopping street and one of the most crowded in Germany. There are four shopping centers in this area: MyZeil, Zeillgalerie, Galeria Kaufhof and Karstadt. *h3* could think to enter in any of these shopping centers.<sup>18</sup> In the city of Munich, *h3* could consider to be present in the following shopping centers: Riem Arcaden<sup>19</sup>, Olympia Einkaufszentrum<sup>20</sup> shopping center and Perlacher Einkaufs Passagen<sup>21</sup>. In Berlin *h3* could enter in Europa Center<sup>22</sup>, Schönhauser Allee Arcaden<sup>23</sup> or Alexa<sup>24</sup> Shopping.

## **Appendix 23: Payments and Duration<sup>25</sup>**

**Nominal fee:** When FPI puts forward an interested party and the franchise system wishes to meet the party based on the confidential report, the first fee is paid by the

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<sup>18</sup> [http://en.wikipedia.org/wiki/Frankfurt#Shopping\\_streets](http://en.wikipedia.org/wiki/Frankfurt#Shopping_streets) (accessed in November 17<sup>th</sup>, 2011)

<sup>19</sup> <http://www.cityscouter.com/travelguides/munich/Riem-Arcaden.html> (accessed in November 17<sup>th</sup>, 2011)

<sup>20</sup> <http://www.cityscouter.com/travelguides/munich/Olympia-Shopping-Centre-OEZ.html> (accessed in November 17<sup>th</sup>, 2011)

<sup>21</sup> <http://www.cityscouter.com/travelguides/munich/PEP-Neuperlach.html> (accessed in November 17<sup>th</sup>, 2011)

<sup>22</sup> [http://www.virtualltourist.com/travel/Europe/Germany/Land\\_Berlin/Berlin-75302/Shopping-Berlin-Europa\\_Center-BR-1.html#ixzz1d7SGJQvz](http://www.virtualltourist.com/travel/Europe/Germany/Land_Berlin/Berlin-75302/Shopping-Berlin-Europa_Center-BR-1.html#ixzz1d7SGJQvz) (accessed in November 17<sup>th</sup>, 2011)

<sup>23</sup> <http://berlin.barwick.de/shopping/centres-and-malls/schoenhauser-allee-arcaden.html> (accessed in November 17<sup>th</sup>, 2011)

<sup>24</sup> <http://berlin.barwick.de/shopping/centres-and-malls/alexa.html> (accessed in November 17<sup>th</sup>, 2011)

<sup>25</sup> Information given by Mr. Rolf Kirst, board member of the International Franchise Affairs and German Franchise Association

franchise system. In the event that the franchise system does not wish to meet the interested party, no costs are incurred. Nominal fee €1,000 per candidate accepted by system to come

**Retainer fee:** A monthly basic payment has to be agreed which will be paid in advance for at minimum 12 months. This covers a range of activities (market observation, interviewing, direct marketing, travel, administration, etc.). Monthly retainer fee of €1,000 in 2011.

**Placement Commission/Success fee:** For each successful placement of a master franchise license, FPI receives a placement commission fee (25% of the master license fee, minimum €30,000). If a smaller area will be arranged in the form of an area developer or a single franchise license will be sold, an adjusted fee has to be paid.

In the event that the partner introduced by FPI acquires a further franchise license in the future from the franchise system (for example for an additional area), FPI will receive 50% of the original placement commission (for a single license FPI charges €12,000 as flat fee).

**Duration:** The contract lasts for 12 months and is automatically extended by an additional year if neither of the two parties withdraws from the contract in writing within the three months preceding the end of the contract. All costs are payable in full within 14 days of the relevant conditions being introduced. The franchise system will make the company information and advertising material available to FPI and FPI free of charge and in sufficient quantities. This offer is non-binding.